



## SOMERLEY CAPITAL LIMITED

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17 November 2015

To: *the Independent Unitholders*

Dear Sirs,

### ONE-OFF REDEMPTION OFFER AND RECURRING REDEMPTION OFFER

#### INTRODUCTION

We refer to our appointment as independent financial adviser to advise the Independent Unitholders on the terms of (i) the One-off Redemption Offer; and (ii) the Recurring Redemption Offer. Details of the One-off Redemption Offer and the Recurring Redemption Offer are set out in the "Letter from the Manager" contained in the circular of the Fund to the Unitholders dated 17 November 2015 (the "**Circular**"), of which this letter forms a part. Capitalised terms used in this letter shall have the same meanings as those defined in the Circular unless the context otherwise requires.

Pursuant to the One-off Redemption Offer, the Manager offers a right to the Unitholders to redeem the whole or a part of their Units for cash (subject to the Redemption Levy) at the net asset value of the Units being redeemed (calculated using the relevant market closing price of the underlying investments of the Fund and the Fund's applicable operating expenses accrued or incurred to date on the Value Day) on the Redemption Day provided that for the Fund as a whole the total number of Units to be redeemed by the Unitholders shall not exceed 20% of the total outstanding number of Units as at the Lodgement Date. The Unitholders are not compelled to accept any such offer and may choose to retain all their Units if they wish.

Pursuant to the Recurring Redemption Offer, the Manager will offer rights to the Unitholders to redeem part or all of their holdings in the Fund for cash (subject to the Redemption Levy) as the Manager determines at its discretion, subject to certain conditions and the Manager's compliance with certain principles and rules as set out in the section related to the Recurring Redemption Offer and the aggregate redemption of the Unitholders to be no more than 20% of the total outstanding number of Units as at the relevant lodgement date of each Recurring Redemption Offer.

The One-off Redemption Offer and the Recurring Redemption Offer are subject to certain conditions as set out in the Circular, in particular, the Independent Unitholders' approval by way of the Extraordinary Resolutions at the General Meeting. The Trustee, the





custodian of the Fund, the Manager and their respective Connected Persons including, fellow subsidiaries and/or associated companies of the Manager as well as the Manager's parent company, the subsidiaries of the Manager's parent company and associated companies of the Manager's parent company and the subsidiaries of such parent company that (i) trade in Units as discretionary fund managers and/or (ii) for proprietary purposes own or control or direct the holding of voting rights and rights over the Units, shall abstain from voting on the Extraordinary Resolutions. Only Independent Unitholders will be entitled to vote on the Extraordinary Resolutions. As at the Latest Practicable Date, the Manager is unaware of any Unitholders (other than those mentioned above, the details of which have been set out in "Appendix 1 — Explanatory Statement — 5. Disclosure of Interests and Dealings" in the Circular) that are required to abstain from voting in respect of the Extraordinary Resolutions proposed at the General Meeting.

An independent committee will not be established to advise the Independent Unitholders. The non-executive directors of the Manager have a potential conflict of interest because (i) they are employees of various subsidiaries of HSBC Holdings plc and (ii) certain fellow subsidiaries and/or associated companies and shareholders of the Manager have traded in the Units for proprietary purposes and/or have undertaken transactions with the Fund such as acting as brokers for the Fund. We, Somerley Capital Limited, have been appointed as the Independent Financial Adviser to advise the Independent Unitholders in respect of the One-off Redemption Offer and the Recurring Redemption Offer as to whether the terms of the One-off Redemption Offer and the Recurring Redemption Offer are fair and reasonable so far as the Independent Unitholders are concerned and on how they should vote at the General Meeting and whether to accept the One-off Redemption Offer and the Recurring Redemption Offer.

Somerley Capital Limited does not have any relationships or interests with the Fund that could reasonably be regarded as relevant to or affect the independence of Somerley Capital Limited. In the last two years, there has been no other engagement between the Fund and Somerley Capital Limited. Accordingly, we do not consider any conflict of interest arises for Somerley Capital Limited in acting as the independent financial adviser of the One-off Redemption Offer and the Recurring Redemption Offer. Apart from normal professional fees paid or payable to us in connection with this appointment as the Independent Financial Adviser, no arrangement exists whereby we will receive any fees or benefits from the Fund.

In formulating our opinion, we have relied on the information and facts supplied, and the opinions expressed, by the Manager's directors, staff and advisers and have assumed that they are true, accurate and complete at the time they were made and will remain so up to the time of the General Meeting. We have also sought and received confirmation from the Manager's directors that all material relevant information has been supplied to us and that no material facts have been omitted from the information supplied and opinions expressed to us. We have no reason to doubt the truth, accuracy or completeness of the information provided to us, or to believe that any material information has been omitted or withheld. We have relied on such information and consider that the information we have received is sufficient for us to reach our advice and recommendation as set out in this letter.





We have, however, not conducted any independent investigation into the business and affairs of the Fund or the Manager, nor have we carried out any independent verification of the information supplied.

## **PRINCIPAL FACTORS AND REASONS CONSIDERED**

In arriving at our opinion and recommendation on whether the terms of the One-off Redemption Offer and the Recurring Redemption Offer are fair and reasonable so far as the Independent Unitholders are concerned, we have taken the following principal factors and reasons into consideration:

### **1. Background information of the Fund**

Launched in July 2007, the Fund is a unit trust constituted by the Trust Deed under Hong Kong law and authorised by the SFC under the SFO. It is an actively managed fund listed on the Main Board of the Stock Exchange and seeks long-term capital growth by investing primarily in A Shares directly through the QFII investment quota of the Manager and indirectly through investment of (i) up to 40% of its net asset value in financial derivative instruments and securities linked to A Shares (such as CAAPs (including A Share participation certificates/notes and/or other access products issued by third party investment banks or brokers)) and (ii) up to 40% of its net asset value in ETFs (including synthetic ETFs) authorised by the SFC with exposure to A Shares, provided that the Fund's total investments in CAAPs and ETFs (including synthetic ETFs) authorised by the SFC with exposure to A Shares will not exceed 50% in the aggregate of the Fund's net asset value.

With the proposed Change of Investment Objective, which is subject to the Independent Unitholders' approval by way of the Extraordinary Resolution at the General Meeting, the Fund may also invest in A Shares through the Stock Connect. Exposure to A Shares through the Stock Connect will not be more than 30% of the Fund's net asset value. The Manager believes that the proposed Change of Investment Objective will provide more flexibility to achieve the investment objective of the Fund with the ability to invest in A Shares from offshore.



## 2. Performance of the Fund

Set out below is the summary of the performance of the Fund for each of the three years ended 31 March 2013, 2014 and 2015 as extracted from the Fund's 2014 and 2015 annual reports:

	For the year ended 31 March		
	2015	2014	2013
	HK\$ (audited)	HK\$ (audited)	HK\$ (audited)
Net investment income/(loss)	1,272,742,147	(76,026,351)	88,785,555
Increase/(decrease) in net assets attributable to the Unitholders and total comprehensive income for the year	1,227,073,814	(123,357,679)	(5,172,840)
	As at 31 March		
	2015	2014	2013
	HK\$ (audited)	HK\$ (audited)	HK\$ (audited)
Total net asset value	2,855,917,483	1,628,843,669	1,752,201,348
Total net asset value per Unit	13.61	7.76	8.35

### (i) 2015 compared to 2014

The Fund recorded an increase in net assets attributable to the Unitholders of approximately HK\$1,227.1 million for the year ended 31 March 2015, compared to a decrease in net assets attributable to the Unitholders of approximately HK\$123.4 million in last year. According to the 2015 annual report of the Fund, the satisfactory performance of Chinese equities for the year ended 31 March 2015 primarily resulted from the launch of Shanghai-Hong Kong Stock Connect on 17 November 2014 and monetary loosening by the People's Bank of China. Accordingly, the total net asset value per Unit of the Fund increased from approximately HK\$7.76 as at 31 March 2014 to approximately HK\$13.61 as at 31 March 2015.

### (ii) 2014 compared to 2013

The decrease in net assets attributable to the Unitholders for the year ended 31 March 2014 was approximately HK\$123.4 million, as compared to the decrease in net assets attributable to the Unitholders of approximately HK\$5.2 million for the year ended 31 March 2013. According to the 2014 annual report of the Fund, this was mainly attributable to a slowdown in economic activities in China resulting from the PRC government's reforms and policies in maintaining stable long-term growth and fear of investors on withdrawal of liquidity from Asia





subsequent to the ultra-loose monetary policy implemented in the United States. As a result, the Fund recorded a decrease in the total net asset value per Unit of the Fund from approximately HK\$8.35 as at 31 March 2013 to approximately HK\$7.76 as at 31 March 2014.

### **3. One-off Redemption Offer**

The Manager proposes to offer the Unitholders the One-off Redemption Offer, which is a right to redeem the whole or a part of their Units. The principal terms and conditions of this offer are set out below:

#### ***(i) Principal terms***

- (a) the Unitholders can apply to redeem the whole or a part of their holdings on the Redemption Day provided that for the Fund as a whole the total number of Units to be redeemed by the Unitholders shall not exceed 20% of the total outstanding number of Units as at the Lodgement Date;
- (b) the One-off Redemption Offer shall occur on the Redemption Day at the net asset value of the Units being redeemed on the Value Day less the Redemption Levy;
- (c) in the event that the total number of Units for which applications are made under the One-off Redemption Offer exceeds 20% of the total outstanding number of Units as at the Lodgement Date, the redemption requests of the Unitholders will be satisfied on a pro rata basis based on the number of Units the Unitholders have validly applied to redeem, rounded down to the nearest whole Unit;
- (d) in the event that the total number of Units for which applications are made under the One-off Redemption Offer is less than or equal to 20% of the total outstanding number of Units as at the Lodgement Date, the Manager shall satisfy all such redemption requests; and
- (e) the Manager shall realise the Fund's offshore assets first to satisfy the redemption requests, subject to the condition that the Manager will aim to ensure that the Fund will continue to hold approximately 5% of the Fund's total net asset value offshore outside the PRC immediately after the redemption. If the amount obtained is not adequate to pay the redemption proceeds, the Manager will realise a portion of the assets of the Fund in the PRC.



**(ii) Conditions to the One-off Redemption Offer**

The One-off Redemption Offer will be subject to certain conditions as set out in the Circular, in particular, the Independent Unitholders' approval by way of an Extraordinary Resolution at the General Meeting to approve the One-off Redemption Offer. The conditions may not be waived.

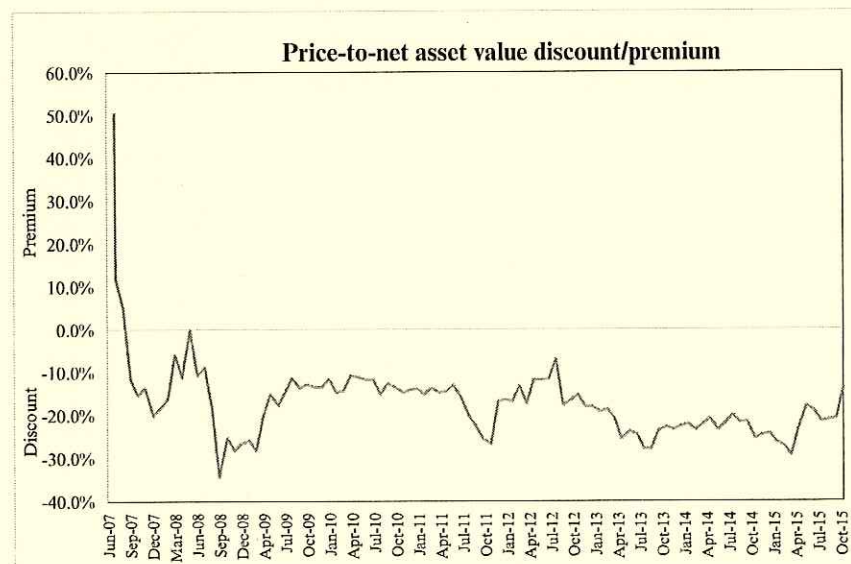
The One-off Redemption Offer will not lapse or be conditional on any minimum number of redemption applications made by the Unitholders.

**(iii) Reasons for the One-off Redemption Offer**

We consider the One-off Redemption Offer is beneficial to the Independent Unitholders in the following aspects:

- (a) The One-off Redemption Offer provides the Independent Unitholders an option to exit a substantial part (or, in certain circumstances, the whole) of their investments in the Fund on the Redemption Day at the net asset value of the Units being redeemed on the Value Day (subject to the Redemption Levy). Given the fact that the Fund has been trading at a discount to its net asset value since October 2007, an opportunity to redeem at the net asset value is in our view advantageous to the Independent Unitholders.

Set out below is a chart showing the discount or premium of the Fund's market price on the Stock Exchange to its monthly net asset value per Unit since it was listed in July 2007.



Source: Bloomberg





As shown in the chart above, the Fund has been trading at a discount to its net asset value since October 2007. After the release of the June 2015 Announcement, the price-to-net asset value discount of the Fund decreased from approximately 23.8% on 17 June 2015 to approximately 20.8% on 18 June 2015 and further to a minimum of approximately 12.7% on 2 July 2015. As at 12 November 2015 (being the last Business Day before the Latest Practicable Date), the price-to-net asset value discount of the Fund is approximately 18.7%.

The Manager offered a right to the Unitholders to redeem the whole or a part of their holdings in the Fund in 2012 (the “**2012 Redemption Offer**”). Subsequent to the 2012 Redemption Offer, the price-to-net asset value discount of the Fund improved from approximately 12.4% on 20 July 2012, the date of issue of the circular in relation to the 2012 Redemption Offer, to a minimum of approximately 5.7% on 30 August 2012. However, the 2012 Redemption Offer was effective in narrowing the discount for a short period only, as the price-to-net asset value discount increased to over 15% one month after the 2012 Redemption Offer and remained at approximately that level for most of the calendar year 2012.

The Fund has been traded at a daily average discount of approximately 23.3%, 22.3% and 23.8% to its net asset value during the calendar year 2013, 2014 and during the nine months ended 30 September 2015, respectively. In our view, a one-off redemption offer tends to improve the price-to-net asset value discount of the Fund for a short period of time, but soon loses effectiveness. However, it is believed that the effect would potentially be sustainable for a continuing period if the Manager is equipped with the power to make the Recurring Redemption Offer in the future on a more frequent basis so as to narrow the price-net-asset value discount. Even so, there is no assurance that the Fund will be traded at a price that is equal to or at a reduced discount to its net asset value subsequent to adopting the Recurring Redemption Offer.

- (b) The One-off Redemption Offer provides an alternative to the Independent Unitholders to diversify their portfolios. For Independent Unitholders who would like to maintain or gain more exposure to non-A Share investments such as B shares and H shares, the One-off Redemption Offer gives them an opportunity to have a part (or, in certain circumstances, the whole) of their Units redeemed at the net asset value and to use such redemption proceeds to invest in securities which they consider appropriate for their investment objectives.





*(iv) Financial effects of the One-off Redemption Offer*

The One-off Redemption Offer, if effected, will reduce the total net asset value, and therefore size, of the Fund by an amount proportionate to the actual number of Units redeemed. It will increase the total expense ratio of the Fund from approximately 1.8% for the financial year ended 31 March 2015 to approximately 2.03% if the One-off Redemption Offer is effected (assuming that 20% of the total outstanding units are being redeemed).

We are of the view that the reduction in the total net asset value, and therefore size, is inevitable given the nature of the One-off Redemption Offer. The increase in the total expense ratio is mainly attributable to the decrease in the size of the Fund after the One-off Redemption Offer and professional and administration expenses to be incurred in the One-off Redemption Offer, the effect is considered to be not material and acceptable. Given that the expenses are incurred to facilitate the launch of the One-off Redemption Offer which is to be given to all the Unitholders with an option to redeem the Units at the net asset value per Unit of the Fund, it is considered to be fair to the Unitholders to bear the relevant expenses. The One-off Redemption Offer will not significantly affect the liabilities of the Fund as the redemption proceeds payable to Unitholders will be satisfied in full by the disposition by the Manager of assets of the Fund.

*(v) Risks associated with the One-off Redemption Offer*

Set out below are the principal risks associated with the One-Off Redemption Offer which we have considered during our assessment of the fairness and reasonableness of the One-off Redemption Offer:

*(a) Uncertainty on the payment date of the redemption proceeds*

The Manager shall use its best endeavours to pay all the redemption proceeds, less the Redemption Levy, within two months after the Redemption Day. The distribution of redemption proceeds payable out of the Fund's assets in the PRC will be subject to the prior approval of SAFE and may be delayed beyond the control of the Manager. There is no assurance that redemption proceeds payable out of the Fund's assets in the PRC will be distributed within two months. The Fund may need to pay the redemption proceeds, less the Redemption Levy, by instalments depending on a number of factors including, but not limited to, the total amount of redemption requests, the amount of offshore assets held by the Fund (i.e. assets outside the PRC), the monthly repatriation limit on the net realised profits and principal funds by QFIIs, the time required by the Fund to repatriate funds from the PRC. According to the legal and regulatory requirements in the PRC, if the Fund is required to repatriate disposition proceeds from the PRC to satisfy the entire or part of the redemption requests accepted by the Fund in respect of the One-off Redemption Offer, the payment of such redemption proceeds under the One-off Redemption Offer is subject to the applicable PRC repatriation rules and the regulatory





and tax clearance approval process which may cause delays or adjustment in calculation of the repatriation limits. For further details, please refer to the section headed “III. One-off Redemption Offer — (b) Key Risk Factors — (i) Uncertainty on the payment date of the redemption proceeds” in the Letter from the Manager of the Circular. We consider the uncertainty on the payment date is acceptable given the current rules and regulations in the PRC on repatriation of assets out of the PRC.

*(b) The net asset value at which the eligible Units are redeemed*

Under the One-off Redemption Offer, the eligible Units will be redeemed at the net asset value on the Value Day. The net asset value per Unit of the Fund on the Value Day cannot be calculated as at the Latest Practicable Date. The net asset value per Unit of the Fund on the Value Day may possibly be lower than the then market price of the Fund on the Stock Exchange, although this has not been the case historically except for a short period just after the Fund’s launch in 2007.

*(c) The actual number of Units eventually redeemed*

A Unitholder may not be able to redeem all the Units he or she applies to redeem under the One-off Redemption Offer regardless of whether he or she applies to redeem more or less than 20% of the Units he or she owns at the Lodgement Date. As stated in the section headed “(i) Principal terms” above, in the event that the aggregate number of Units for which applications are made under the One-off Redemption Offer exceeds 20% of the total outstanding number of Units as at the Lodgement Date, the Manager shall apply the relevant realisation proceeds to satisfy the redemption requests of the Unitholders wishing to redeem their Units on a pro rata basis based on the number of Units they have validly applied to redeem, rounded down to the nearest whole Unit.

*(d) Existence of odd lot Units*

Any Units held by the Unitholders that are not successfully redeemed under the One-off Redemption Offer may be in odd lots, the realisable price of which may be significantly lower than the traded price for such Units on the market.

*(e) Impact on the total expense ratio and size of the Fund*

The One-Off Redemption Offer, (i) if implemented, would increase the total expense ratio of the Fund as a result of the expenses to be incurred with respect to the One-off Redemption Offer and such expenses are not covered by the Redemption Levy; and (ii) would reduce the size of the Fund after such One-off Redemption Offer is implemented. The Manager may decide to terminate the Fund on any date if on such date the asset value of the Fund shall be less than HK\$400,000,000 under the Trust Deed. Based on the



Fund's net asset value as at 12 November 2015 (being the last Business Day before the Latest Practicable Date), the net asset value of the Fund immediately after the One-off Redemption Offer (assuming that 20% of the total outstanding units are being redeemed) would be approximately HK\$2,131,501,095. As advised by the Manager, the reduction of fund size subsequent to the One-off Redemption Offer will not trigger the termination of the Fund.

*(vi) Evaluation of the principal terms of the One-off Redemption Offer*

*(a) Percentage of the Fund's net asset value to be redeemed*

Under the One-off Redemption Offer, there is no minimum number of Units which a Unitholder can apply to redeem. A Unitholder may apply to redeem the whole or a part of his or her holding of Units. However, the total number of Units to be redeemed by the Unitholders shall not be more than 20% of the total outstanding number of Units as at the Lodgement Date.

According to current rules and regulations in the PRC, net realised profits and principal funds of the QFII, up to 20% of the QFII's total asset value in the PRC as of the end of the immediately preceding calendar year, may be repatriated out of the PRC on a monthly basis, subject to the relevant regulatory approval and the satisfaction of required documents (where applicable).

The limit of 20% of the Fund's net asset value to be redeemed has been determined by the Manager with reference to the monthly percentage allowed for repatriation out of the PRC under the QFII regulations, which is no more than 20% of the QFII's total asset value in the PRC of the Fund as of the end of the immediately preceding calendar year. As A Shares invested directly through QFII and other net assets in the PRC account for approximately 84% of the net asset value of the Fund as of 12 November 2015, and the Fund is required to repatriate disposition proceeds from the PRC to satisfy part of the redemption requests in respect of the One-off Redemption Offer, the 20% limit has been determined accordingly. On such basis, we consider the maximum redemption percentage of the One-off Redemption Offer appropriate.

*(b) Redemption price*

Under the One-off Redemption Offer, each Unit will be redeemed at the net asset value per Unit of the Fund on the Value Day, subject to the Redemption Levy (as discussed below). The net asset value per Unit is arrived at by valuing the assets of the Fund, deducting the liabilities of the Fund and dividing the net assets by the number of Units in issue. Since the net asset value per Unit is the maximum amount the Unitholders are entitled





to and can receive from the Fund in the event that the Fund divests all of its investments and distributes all of the proceeds to the Unitholders, we consider the basis of the redemption price fair and reasonable.

*(c) Maximum redemption levy*

Under the One-off Redemption Offer, the Manager will pay the Unitholders the net asset value of the eligible Units to be redeemed on the Value Day less a redemption fee of up to 2% of the redemption price. The Redemption Levy, which will be deducted from the redemption price, incorporates explicit transaction costs (e.g. commission and stamp duty) and implicit costs (i.e. market impacts of implementation) incurred in the sale of the underlying investments of the Fund, and will be retained for the benefit of the Fund. Market impacts of implementation are indirect costs resulting from price slippage when orders are executed as there may be a difference between the execution price and the price at the time of valuation. As the explicit transaction costs and implicit costs are incidental to the One-off Redemption Offer, it is reasonable that the costs are to be borne by the Unitholders who accept the One-off Redemption Offer.

AsianInvestor has ranked the top 100 fund management companies in terms of asset under management ("AUM") sourced from Asia Pacific as at 31 December 2014. Among the top 30 fund management companies, we, on a best endeavours basis, identified eleven fund management companies which have launched umbrella funds, consisting of sub-funds investing in China-related securities, for retail sales in Hong Kong, and reviewed their prospectuses. Out of these eleven fund management companies, eight will charge a maximum redemption levy ranging from 1% to 3% (among which six will charge a redemption levy of up to 2%), one will charge a redemption levy ranging from 0% to 4% (subject to the length of holding) and two do not charge any redemption levy at all. As the total AUM of the top 30 fund management companies ranked by AsianInvestor accounts for approximately 68.7% of the AUM of the top 100 fund management companies, and a majority of the top 30 fund management companies (which have launched sub-funds investing in China-related securities for retail sales in Hong Kong) charge a maximum redemption levy with a range from 1% to 3%, we consider the charge of the Redemption Levy is in accordance with the market practice.

The One-off Redemption Offer to be approved by the Independent Unitholders is similar to the 2012 Redemption Offer. Under the 2012 Redemption Offer, a redemption levy of up to 2% of the net asset value of the Units being redeemed was charged, which was in accordance with the then market practice. Given that (i) the range of the Redemption Levy charged for the One-off Redemption Offer is in accordance with the market



practice now and is the same as the range charged for the 2012 Redemption Offer; and (ii) the nature of the two offers and the related redemption levies are similar, we consider that the Redemption Levy is acceptable.

#### 4. Recurring Redemption Offer

The principal terms and conditions of the Recurring Redemption Offer are set out below:

##### *(i) Principal terms and conditions*

- (a) subject to certain conditions as set out in the Circular, in particular, the passing of the proposed resolutions for the Recurring Redemption Offer and the changes to the Trust Deed to effect the Recurring Redemption Offer, the Manager will offer rights to the Unitholders to redeem part or all of their holdings in the Fund as the Manager determines at its discretion taking into account the best interests of the Unitholders, subject to the following conditions;
  - (i) the Fund must be trading at a discount of its net asset value of 20% (daily average) or more for three consecutive months;
  - (ii) the redemption offer must only be made in the best interests of the Unitholders;
  - (iii) there is no material adverse impact to the Fund;
  - (iv) the Manager must comply with the principles and rules under the Code on Share Buy-backs (the “**Share Buy-backs Code**”) as if they were applicable to the Fund (including but not limited to all relevant timing and disclosure requirements under the Share Buy-backs Code), the SFC Products Handbook and all other applicable codes, rules, regulations and laws (together the “**Applicable Regulations**”), with the only following exceptions:
    - (1) no independent advice by an independent board committee and/or independent financial adviser will be required in relation to any redemption offer made following the approval of the Recurring Redemption Offer at the General Meeting;
    - (2) where the redemption proceeds cannot be repatriated from mainland China due to legal or regulatory requirements beyond the control of the Manager, the redemption proceeds payment period may be extended beyond the time limits stipulated in the Applicable Regulations. In such case, the Manager must keep proper records to demonstrate and justify this and keep the Unitholders and the SFC properly and





promptly informed. In any event, the redemption proceeds must be paid to the Unitholders as soon as possible after the receipt of the proceeds by the Fund;

- (v) in considering whether to proceed with a redemption offer, the Manager must take into account of all relevant prevailing market conditions (such as market liquidity, the percentage of stocks held by the Fund which have been suspended from trading and other relevant regulatory requirements) and must be reasonably satisfied that the redemption proceeds can be paid to the Unitholders in accordance with the time limits stipulated in the Applicable Regulations;
  - (vi) there is no minimum number of redemption offer to be made in a calendar year and the maximum number for each calendar year shall not exceed three;
  - (vii) the aggregate redemption of all Unitholders to be no more than 20% of the total outstanding number of Units as at the relevant lodgement date of each Recurring Redemption Offer;
  - (viii) Independent Unitholders may by Extraordinary Resolution at a general meeting terminate the Manager's entitlement to make any further redemption offer under the Recurring Redemption Offer;
- (b) subject to the passing of the proposed resolutions for the Recurring Redemption Offer and the changes to the Trust Deed to effect the Recurring Redemption Offer, each Recurring Redemption Offer will not be subject to any further approval of the Unitholders nor the advice of the independent financial adviser; and
- (c) each Recurring Redemption Offer shall be made as the Manager determines at its discretion at the net asset value of the Units being redeemed (calculated using the relevant market closing price of the underlying investments of the Fund and the Fund's applicable operating expenses accrued or incurred to date on the relevant value day) on the relevant redemption day, subject to the Redemption Levy.

***(ii) Reasons for the Recurring Redemption Offer***

The Recurring Redemption Offer provides an option for the Unitholders to exit the whole or a substantial part of their Units on a more frequent basis at the net asset value per Unit of the Fund, less the Redemption Levy. As set out in the section headed "3. One-off Redemption Offer — (iii) Reasons for the One-off Redemption Offer", the Fund has been traded at a discount to its net asset value since October 2007. In our view, the Recurring Redemption Offer may potentially narrow such discount as the Unitholders will have more opportunities to realise certain Units at the net asset value, less the Redemption Levy. Independent





Unitholders will also be provided with an alternative to diversify their portfolios from time to time if they would like to maintain or gain more exposure to non-A Share investments. As such, we consider the Recurring Redemption Offer is beneficial to the Independent Unitholders.

***(iii) Financial effects of the Recurring Redemption Offer***

The Recurring Redemption Offer, if effected, will further reduce the size of the Fund. Under each Recurring Redemption Offer, additional professional and administration costs will be incurred. Hence, there will be a proportionate increase in the total expense ratio. Assuming that the One-off Redemption Offer and two Recurring Redemption Offers have taken place in a year with 20% of the total outstanding Units on each of the relevant lodgement date being redeemed in full with respect to the One-off Redemption Offer and two Recurring Redemption Offers (that is, 48.8% of the total outstanding Units in issue before all such redemption offers being redeemed in total), this will increase the total expense ratio of the Fund from approximately 1.8% for the financial year ended 31 March 2015 to approximately 2.30% after the One-off Redemption Offer and two Recurring Redemption Offers, the effect on the total expense ratio is considered to be not material and acceptable. As discussed in the section headed “3. One-off Redemption Offer — (iv) Financial effects of the One-off Redemption Offer”, it is considered to be fair to the Unitholders to bear the expenses required for the launch of each Recurring Redemption Offer on the same basis.

***(iv) Risks associated with the Recurring Redemption Offer***

The principal risks associated with the Recurring Redemption Offer which we have considered during our assessment of the fairness and reasonableness of the Recurring Redemption Offer include risks associated with the One-off Redemption Offer, in particular, the risks that (i) the Manager may decide to terminate the Fund on any date if on such date the asset value of the Fund shall be less than HK\$400,000,000, resulting from subsequent Recurring Redemption Offers; and (ii) it may take two months or more for the Unitholders to receive the redemption proceeds for Units redeemed through each Recurring Redemption Offer. Please refer to the section headed “3. One-off Redemption Offer — (v) Risks associated with the One-off Redemption Offer” for further details. Additional risk factors, if any, will be set out in the circular to the Unitholders prior to each Recurring Redemption Offer, mainly as a result of changing market environment and/or changing regulatory requirements.

***(v) Evaluation of the principal terms of the Recurring Redemption Offer***

***(a) Recurring Redemption Offer on a more frequent basis***

The Recurring Redemption Offer represents an offer on a more frequent basis to the Unitholders to redeem a part or all of their holdings in the Fund if they find the investment objectives of the Fund are not aligned with their own investment objectives. With the reasons discussed in the section headed





“4. Recurring Redemption Offer — (ii) Reasons for the Recurring Redemption Offer” and taking into account that the Recurring Redemption Offer gives the Unitholders an option to exit their investments in the Fund at the applicable net asset value of the Fund, less the Redemption Levy, it is considered that the Recurring Redemption Offer is advantageous to the Unitholders.

*(b) the Manager's discretion as regards the Recurring Redemption Offer*

We note that the making of the Recurring Redemption Offer is subject to the Manager's discretion, subject to certain conditions, including but not limited to,

- (i) discount of the Fund to its net asset value. Each Recurring Redemption Offer will only be made when the Fund is trading at a discount to its net asset value of 20% (daily average) or more for three consecutive months. Given the Fund has been trading at a daily average discount of approximately 23.3%, 22.3% and 23.8% to its net asset value during the calendar year 2013, 2014 and the nine months ended 30 September 2015, the discount of 20% is considered reasonable as a benchmark for the making of each Recurring Redemption Offer;
- (ii) compliance with the Share Buy-backs Code and the Applicable Regulations, with the exception of, among others, no further opinion needs to be sought from the independent financial adviser if approval regarding the Recurring Redemption Offer could be obtained from the Independent Unitholders at the General Meeting, and given the unique nature of the Fund, we consider the Manager's compliance with the Share Buy-backs Code and the Applicable Regulations would be in the interests of the Unitholders and no further opinion from the independent financial adviser is necessary if approval could be obtained at the General Meeting;
- (iii) all relevant prevailing market conditions (such as market liquidity, the percentage of stocks held by the Fund which have been suspended from trading; and other relevant regulatory requirements). Given the market fluctuations in recent years and that the market conditions have an impact on realisation of assets by the Fund, it is considered reasonable for the Manager to take into account the market conditions before making each Recurring Redemption Offer; and
- (iv) Independent Unitholders may by Extraordinary Resolution at a general meeting to terminate the Manager's entitlement to make any further redemption offer under the Recurring Redemption Offer. Such condition is in the interests of the Unitholders as they are given the right to terminate the Recurring Redemption Offer.



Given above, we consider that it is reasonable for the Manager to exercise its discretion, subject to the conditions (as analysed immediately above), at the time when determining whether each Recurring Redemption Offer should be made.

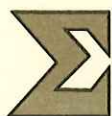
*(c) Redemption limit, redemption price and maximum redemption levy*

The maximum redemption percentage of each Recurring Redemption Offer is 20% of the outstanding number of Units as at the relevant lodgement date of each Recurring Redemption Offer. As analysed in the section headed “3. One-off Redemption Offer — (vi) Evaluation of the principal terms of the One-off Redemption Offer — (a) Percentage of the Fund’s net asset value to be redeemed”, given the monthly repatriation limit of 20% under QFII regulations for funds repatriated from the PRC and that the majority of the Fund’s investments are invested directly through QFII, we consider the maximum redemption percentage of each Recurring Redemption Offer appropriate. As advised by the Manager, given the administrative procedures involved in each redemption offer, the maximum number of redemption offers for each calendar year shall not exceed three. Taken into account the logistic practicality of the redemption offers, we consider it is reasonable for the Manager to determine three as the maximum number of redemption offers for each calendar year.

Under the Recurring Redemption Offer, each Unit will be redeemed at its net asset value on the relevant redemption day, subject to the Redemption Levy (as further discussed in the next paragraph). Since the net asset value per Unit is the maximum amount the Unitholders are entitled to and can receive from the Fund in the event that the Fund divests all its investments and distributes all of the proceeds to the Unitholders, we consider the basis of the redemption price is fair and reasonable.

Based on our analysis in the section headed “3. One-off Redemption Offer — (vi) Evaluation of the principal terms of the One-off Redemption Offer — (c) Maximum redemption levy” above, we consider the Redemption Levy, which is up to 2% of the redemption price, acceptable from the point of view of the Independent Unitholders as it represents the upper limit of the redemption fee that could be charged and is in accordance with present market practice now. Regardless of actual explicit transaction costs and implicit costs to be incurred, a fee of 2% would be the maximum fee that would be borne by the Unitholders for the Recurring Redemption Offer, and a lower level of the Redemption Levy may be charged based on actual costs incurred.





## DISCUSSION AND ANALYSIS

The One-off Redemption Offer is expected to bring the following benefits to the Independent Unitholders:

- (i) it provides the Independent Unitholders with an option to exit a substantial part (or, in certain circumstances, the whole) of their investments in the Fund and to realise Units at the net asset value of the Units being redeemed, less the Redemption Levy. We consider this advantageous to the Independent Unitholders, given that the Fund has been traded at a significant discount to its net asset value since October 2007;
- (ii) it allows the Independent Unitholders to apply the redemption proceeds in purchasing securities which they consider appropriate. On the other hand, should the Fund's investment objective be acceptable to the Independent Unitholders, the Independent Unitholders can choose not to exercise the right under the One-off Redemption Offer and allow the Manager to continue to invest for them; and
- (iii) the redemption price represents the maximum amount the Independent Unitholders are entitled to and can receive from the Fund in the case of redemptions.

Taking into account the above factors, we consider it is in the interests of the Independent Unitholders to approve the One-off Redemption Offer.

The Recurring Redemption Offer is considered to be fair and reasonable to the Independent Unitholders, given that:

- (i) it represents a more frequent option for Independent Unitholders to exit their investments in the Fund at the applicable net asset value per Unit of the Fund;
- (ii) it is reasonable for the Manager to exercise its discretion (the criteria for the exercise of such discretion may include, without limitation, the average discount at which the Units have been trading, the market conditions and any relevant regulatory requirements) for making each Recurring Redemption Offer;
- (iii) the redemption price represents the maximum amount the Independent Unitholders are entitled to and can receive from the Fund in the case of redemptions;
- (iv) the Unitholders may choose not to exercise the right to redeem under each Recurring Redemption Offer if the Fund's investment objective is appropriate for their own investment objectives; and
- (v) the Recurring Redemption Offer, coupled with the One-off Redemption Offer, is likely to be effective in potentially narrowing the price-to-net asset value discount of the Fund, on a long-term basis.





Taking into account the above factors, we consider it is in the interests of the Independent Unitholders to approve the Recurring Redemption Offer.

Meanwhile, the Independent Unitholders should be aware of the risks associated with the One-off Redemption Offer and the Recurring Redemption Offer as discussed in the sections headed “3. One-off Redemption Offer — (v) Risks associated with the One-off Redemption Offer” and “4. Recurring Redemption Offer — (iv) Risks associated with the Recurring Redemption Offer”, including but not limited to, (i) the Manager may decide to terminate the Fund on any date if on such date the asset value of the Fund shall be less than HK\$400,000,000 under the Trust Deed; and (ii) the Unitholders should take into account their liquidity needs as it may take two months or more for the Unitholders to receive the redemption proceeds for Units redeemed through One-off Redemption Offer and each Recurring Redemption Offer while proceeds can be received immediately by selling their Units in the open market.

#### **RECOMMENDATION**

Taking into account the above principal factors and reasons (including but not limited to, the terms and conditions), we consider that the terms of the One-off Redemption Offer and the Recurring Redemption Offer are fair and reasonable so far as the Independent Unitholders are concerned, and are in the interests of the Independent Unitholders as a whole. Accordingly, we recommend the Independent Unitholders to vote in favour of the Extraordinary Resolutions to be proposed at the General Meeting to approve, among other things, the One-off Redemption Offer and the Recurring Redemption Offer.

If the Independent Unitholders consider the Fund’s investment objective appropriate for their own investment objectives and willingness to assume risk taking into account the market price now, they may choose not to accept the One-off Redemption Offer or each Recurring Redemption Offer and allow the Manager to continue to invest for them.

If the Independent Unitholders now consider the Fund’s investment objective inappropriate for their own investment objectives and willingness to assume risk of their investments taking into account the market price, or if they would like to maintain less exposure to A Share investments now, they should consider accepting the One-off Redemption Offer or each Recurring Redemption Offer if the net proceeds from the market sale of their Units after deducting all transaction costs are less than the net proceeds to be received under the One-off Redemption Offer or each Recurring Redemption Offer at that time and using such redemption proceeds to invest in securities which they consider appropriate for their own individual circumstances.

The Independent Unitholders should reassess their positions at the time when each Recurring Redemption Offer is made to them.

Independent Unitholders should note that although the Fund has been traded at a discount to its net asset value since October 2007, it is in principle possible that the Fund could be traded above its net asset value when the One-off Redemption Offer or each Recurring Redemption Offer occurs. As such, it is advisable for the Independent Unitholders to consider, should they wish to liquidate their holdings, selling their Units





in the open market rather than through the One-off Redemption Offer or each Recurring Redemption Offer if the market price of the Units exceeds the net asset value per Unit, or the net proceeds from the market sale of their Units after deducting all transaction costs are more than the net proceeds to be received under the One-off Redemption Offer or each Recurring Redemption Offer at that time.

Yours faithfully,  
for and on behalf of  
**SOMERLEY CAPITAL LIMITED**



**David Ching**  
Director

*Mr. David Ching is a licensed person registered with the Securities and Futures Commission and a responsible officer of Somerley Capital Limited, which is licensed under the SFO to carry out Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities. He has over ten years of experience in the corporate finance industry.*